



To: Board of Finance
From: Katherine Schad, Chief Administrative Officer
Richard Goodwin, Director of Financial Operations
Re: FY20 Fiscal Health Report
Date: February 1, 2021

Below is the annual fiscal health report for the City of Burlington. Please note that due to the transition of the Chief Administrative Officer and the COVID pandemic the Clerk/Treasurer's Office did not issue a FY19 report but we are pleased to resume the practice at this time.

Over the past six years, the City has realized significant improvement in its overall financial condition because the Administration, Department Heads and all City staff, and the City Council made a commitment to improving the City's financial position. This report provides information about the steps that the City took to improve its financial standing and the impacts of those efforts.

The City's Credit Rating

The City of Burlington receives regular reviews by bond credit rating firm Moody's, which performs a thorough analysis of the City's finances. Moody's assigns a credit score to the City and this score is used by financial institutions to understand the relative risk of lending money to Burlington. A better score is important because it leads to lower interest rates and more preferable terms, saving taxpayers money.

A Credit Crisis

Between 2010 and 2012, the City's credit rating was downgraded six steps in three separate actions by Moody's, from a high of Aa3 to a low of Baa3, only one step from junk bond status. Moody's cited the Burlington Telecom liability and advances to other enterprise funds; increasing reliance on short-term borrowing; and multiple years of operating deficits as key reasons for the downgrades. Further, in FY12 the Management Letter from the City's auditor stated the City was "at risk" due to being "overly reliant on borrowing from financial institutions to provide overall City short-term cash requirements."

In response, and as a foundation for improving the City's fiscal picture, the Mayor and City Council received voter approval to issue \$9 million in Fiscal Stability Bonds in 2013. The bond proceeds resulted in an immediate improvement of the City's cash situation and eliminated costly short-term borrowing.

Upgraded to an A

Since the June 2012 downgrade and the 2013 Fiscal Stability Bond issuance, the City has seen four credit rating upgrades **for a total of a six-notch improvement with the most recent upgrade to Aa3 being achieved in July 2019 and maintained since¹.**

Moody's has pointed to the following for Burlington's improved rating:

- Strong City of Burlington management team
- Operating surpluses in recent budget years
- Elimination of short-term borrowing
- Creating and following fund balance policy
- Developing a multi-year capital improvement program
- Stable underlying economy and tax base serving as the economic center of the state
- Strong reserve levels and cash position; and
- Elimination of risks associated with Burlington Telecom litigation.

Impact to Citizens

An improved credit rating has real impacts on the City and its citizens because it is much cheaper to borrow money with an Aa3 rating than with a Baa3 rating.

We have estimated the actual cost of debt service for all bonds issued after the Fiscal Stability Bond to the cost of what those bonds would have been if they had been issued at the Baa3 negative outlook bond rating². **The City has locked in an estimated \$21,203,967³ in current dollars of savings, over the terms of the bonds, a direct savings for each taxpayer and rate payer.**

Please note that while the Fiscal Stability Bond is not the only reason for the creation of these savings, it was the first key step in this process.

The General Fund Unassigned Fund Balance (also known as The Rainy-Day Fund)

The unassigned fund balance (UAFB) is an important reflection of the City's financial health because it ensures we have the appropriate liquidity to support City operations, cover debt service obligations, and to respond to unforeseen events, such as the COVID-19 pandemic. Further, our fund balance is a direct component of how Moody's assigns its ratings.

The City's [Fund Balance Policy](#) establishes a target level for the UAFB as a minimum of 5% and a maximum of 15% of the City's General Fund operational costs, with a preference for staying in the 10-15% range.

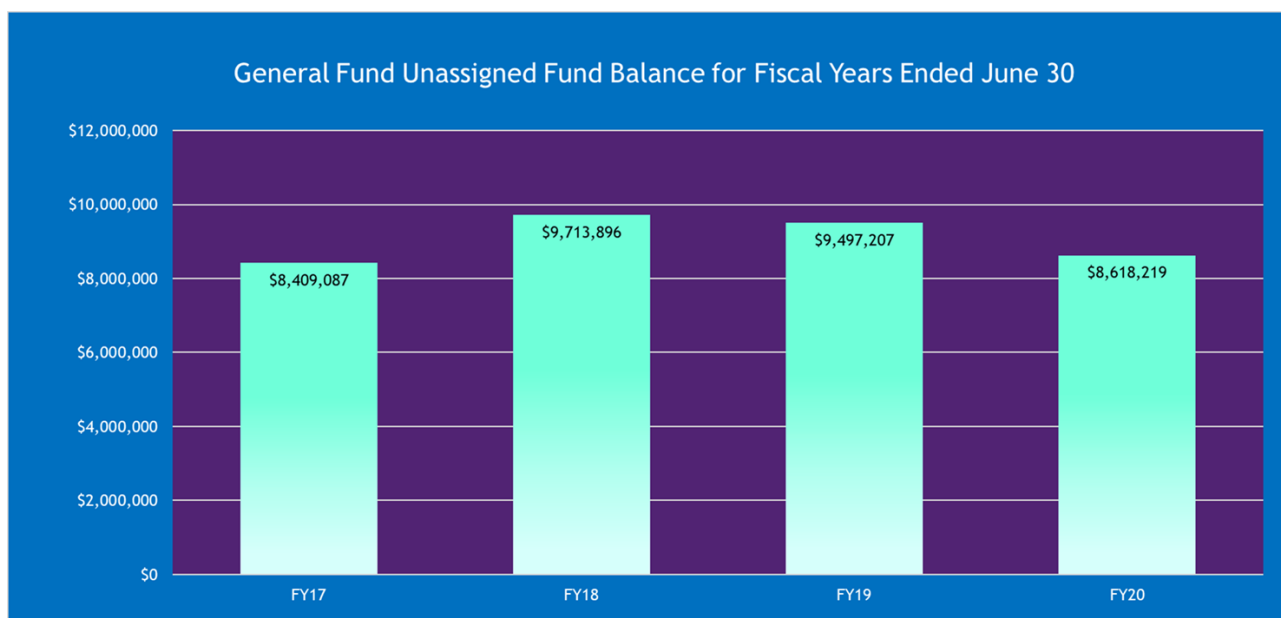
¹ Please see "Looking Ahead" section for how the City can further increase this rating

² The estimated savings are detailed in the attached spreadsheets, which include the borrowing terms of each bond issued during the timeframe, and the discount rate used to estimate current savings.

³ This represents \$30,150,830 in total dollars, not discounted to current value.

Preparing for the Storm

In FY12 the City had a negative UAFB, primarily driven by the uncollectible Burlington Telecom receivable. This means that there was no rainy-day fund at all for the City. As stated above, the first step to stabilize the situation was issuing \$9 million in Fiscal Stability Bonds. Then the Administration and leadership team worked hard over many years to focus on fiscal management while also still implementing innovative and new programming. As a result, you can see in the chart below that by FY17 the City had over \$8M set aside in case it was needed for a crisis. This rainy-day fund has remained stable over the past four years, with balances remaining well above 10% of operational costs over the past several years. The balance for FY20 shows a small \$878,988 decrease in the fund balance compared to FY19, which is the result of COVID-related shortfalls in revenues. This still leaves the City with a strong balance of \$8.6M in its rainy-day fund.



Impact to Citizens

When the pandemic hit and municipal revenues around the U.S. collapsed, many cities were forced to furlough staff or cut jobs altogether, thereby severely curtailing services available to citizens. With the security of Burlington's carefully maintained UAFB or rainy-day fund, the City was able to continue to provide the services our citizens rely on and also to dedicate \$1M to additional Citywide COVID relief.

Looking forward

Burlington now has re-established its highest credit rating ever of Aa3. The most recent Moody's report, issued in November 2019, suggested that "reduction in debt levels and pension liabilities" could lead to a further rating increase.

At the Mayor's request, our financial advisors assessed the City's financial status and recommended a number of steps for us to take to help achieve additional ratings increases.⁴ Those recommendations, and an update on the action that we have taken on each, follows:

- **Recommendation:** Settle on a final favorable resolution to the BT case
Action: In March 2019, the City closed on the sale of Burlington Telecom (BT) to Schurz Communications. The closing brought full and final resolution to a \$33.5+ million lawsuit with Citibank, with Citibank's full release of the City from further BT liability. The closing resulted in a recovery of over \$6.4 million of the \$17 million spent by the City on BT. Resolution of the BT lawsuit and the subsequent transfer of BT is one of the major steps taken by the City to improve its credit rating.
- **Recommendation:** Continue to minimize enterprise risk through satisfactory management of the operations and fiscal performance of the City enterprise funds which will insulate the General Fund from any exposure.
Action:
 - Burlington Electric Department has maintained a Moody's A3 credit rating with a stable outlook since 2016. Moody's June 2019 credit opinion cited BED's 100% renewable, diverse power supply, robust service area economy, and strong management focus on ensuring utility fixed cost recovery through rates during an industry transition as key strengths. BED's FY20 results were slightly improved compared to FY19 despite the impacts of COVID-19.
 - Burlington International Airport received a rating upgrade from Moody's in May 2018 to Baa2 and Fitch in September 2018 to BBB. Both rating agencies have continued to affirm these ratings since that time, which is especially remarkable in light of the slowdown in air travel surrounding COVID-19.
 - The Administration and leadership team continue to focus on sound budgeting and financial performance across all City departments, including enterprise funds and special revenue funds. This is evidenced by the strong credit ratings of the enterprise funds and solid budget performance of departments.
- **Recommendation:** Consider adopting a Debt Policy & Capacity Model that would outline acceptable thresholds, ratios and target levels for debt.
Action: In September 2019, the City Council, in collaboration with the Burlington School Department, approved a [Debt Policy](#) that sets limits for the amount and type of debt the City can undertake to ensure the responsible management of debt and its impact on taxpayers. The City has followed this policy since its inception.
- **Recommendation:** Analyze the economic benefits of refunding the City's 2013 Stabilization bonds.
Action: The Clerk/Treasurer's Officer explored this option with our financial advisor, but found that it was not a cost-effective action at current market rates.

⁴ See [PFM memo](#) dated December 12, 2017

- **Recommendation:** Initiate annual benchmarking and peer group analysis.
Action: Based on this feedback, the Clerk/Treasurer's Office and City's financial advisor built financial models to ensure our anticipated debt load will still result in an "A" credit rating. The financial models allow the City to run various scenarios helping to inform policy makers, staff, and stakeholders of the potential rating impacts of policy decisions being contemplated (change in debt load, revenue, expenditures, fund balance or pension liability). The City's financial advisor has also provided benchmarking to a number of peer cities throughout the country to ensure that we are on track when measured against a comparable group.

Closing

In summary, over this past year the City has continued to achieve significant savings as a result of its improved fiscal management and health. That said, financial challenges for the City certainly remain. As mentioned in the CAO's recent FY22 budget update to BOF, the early forecast shows an expected shortfall in City revenue due to the ongoing pandemic. The Administration plans to implement the \$.03 public safety tax increase passed (but not implemented) in March 2020 but not to raise taxes further to solve this deficit, understanding this is a difficult time for many of Burlington's citizens. Instead we will continue to pursue State and Federal relief, revise conservative revenue projections as appropriate, and work with Department Heads to deliver a balanced budget without cutting City programs or staff.

We remain optimistic about the financial health of the City of Burlington. The UAFB remains high and the savings we have achieved as a result of our high credit rating are significant. These are a direct result of the commitment and leadership of the Mayor and the City Council, as well as the continued efforts of all of the City departments. Moreover, this plan has succeeded because Burlington voters have consistently supported this focus with multiple votes over the last six years. We believe that through continued responsible financial management, maintaining the unassigned fund balance, and identifying new sources of efficiencies, we can achieve further ratings upgrades and additional reductions in our debt service costs, keeping Burlington strong for generations to come.